CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

May 10, 2000

H.R. 4030
Enhancement of Military Benefits Act

As introduced on March 16, 2000

SUMMARY

H.R. 4030 would increase various elements of compensation for current members of the uniformed services, retired members, and their survivors. Specifically, it would increase pay for military personnel and change the current demonstration project of Medicare subvention to a permanent, nationwide program. It also would allow retirees of the uniformed services, their dependents, and surviving spouses to enroll in the Federal Employees Health Benefits program (FEHB). H.R. 4030 also would repeal the current reduction in uniformed services survivor annuities that occurs when the survivors become eligible for survivor benefits under Social Security.

CBO estimates that implementing the bill would cost $690 million in 2001 and about $3.8 billion over the 2001-2005 period, assuming appropriation of the necessary amounts. Enacting the bill would raise direct spending by about $1.9 billion in 2001 and by about $21 billion over the 2001-2005 period. Because the bill would affect direct spending, pay-as-you-go procedures would apply.

The bill contains private-sector and intergovernmental mandates; however, the costs of those mandates would not exceed the thresholds specified in the Unfunded Mandates Reform Act (UMRA).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 4030 is shown in Table 1. The direct spending costs of this legislation would fall within budget functions 550 (health), 570 (Medicare), 600 (income security), 300 (natural resources and environment), and 400 (transportation). The spending subject to appropriation would fall within budget function 050 (national defense).

TABLE 1. ESTIMATED COSTS OF H.R. 4030

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
CHANGES IN DIRECT SPENDING						
Estimated Budget Authority	0	1,913	3,327	4,738	5,392	5,822
Estimated Outlays	0	1,913	3,327	4,738	5,392	5,822
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Estimated Authorization Level	0	696	810	764	763	782
Estimated Outlays	0	690	817	776	771	786

Direct Spending

The bill would raise direct spending from provisions on health coverage under FEHB, Medicare subvention, and survivor benefits. The impact of those provisions on direct spending is detailed in Table 2.

Costs of Premium Payments Under FEHB. Under current law, military retirees under the age of 65 are eligible either to enroll in the Department of Defense's (DoD's) managed care program (Tricare Prime) or to use its insurance programs (Tricare Standard or Extra), which do not require enrollment. Those who use Tricare Standard or Extra may also seek care at military treatment facilities (MTF) on a space-available basis. Once retirees turn age 65, they are no longer eligible to use Tricare, though they may continue to seek care at MTFs when space is available. The same eligibility rules apply to survivors, who are primarily widows and widowers.

Section 5 of H.R. 4030 would allow greater access to health insurance by allowing all retirees and their dependents the opportunity to enroll in FEHB. (The bill states that retirees and dependents would be eligible to enroll in FEHB; it does not explicitly say that survivors would be eligible. CBO assumes that the bill would also allow retirees' survivors to participate in FEHB because the bill would not prohibit their participation and because DoD could interpret the reference to dependents to include survivors.) All retirees would continue to be able to use MTFs for health care on a space-available basis. The bill would result in additional costs for spending on FEHB premiums and increased use of Medicare, but there would be a decrease in the costs of Tricare. (Also see the discussion of spending subject to appropriation.)

DoD's contribution toward FEHB premiums for beneficiaries under H.R. 4030 would cost $1.2 billion in 2001, $15.7 billion over the 2001-2005 period, and $43 billion over the 2001-2010 period. Coverage for beneficiaries over age 64 would constitute about 60 percent of the total cost of this provision.

TABLE 2. ESTIMATED DIRECT SPENDING UNDER H.R. 4030

	By Fiscal Year, Outlays in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
DIRECT SPENDING						
Costs of Premium Payments Under FEHB						
Spending Under Current Law	5,012	5,456	5,906	6,352	6,826	7,338
Proposed Changes	0	1,200	2,400	3,600	4,100	4,400
Spending Under H.R. 4030	5,012	6,656	8,306	9,952	10,926	11,738
Cost Increases in Medicare						
Spending Under Current Law	195,113	211,518	217,077	234,887	250,997	274,149
Proposed Changes						
FEHB Coverage	0	150	290	420	490	530
Medicare Subvention	0	20	35	55	75	100
Subtotal-Proposed Changes	0	170	325	475	565	630
Spending Under H.R. 4030	195,113	211,688	217,402	235,362	251,562	274,779
Cost Increases in Uniformed Services Retirement [a]						
Spending Under Current Law	33,614	34,540	35,407	36,379	37,436	38,644
Proposed Changes	0	543	602	663	727	792
Spending Under H.R. 4030	33,614	35,083	36,009	37,042	38,163	39,436
Total Proposed Changes						
Estimated Budget Authority	0	1,913	3,327	4,738	5,392	5,822
Estimated Outlays	0	1,913	3,327	4,738	5,392	5,822

a. Uniformed Services Retirement includes some spending in budget functions 600 (income security), 300 (natural resources and environment), 400 (transportation), and 550 (health).

Eligible Population and Participation Rates. Using data from the DoD, CBO estimates that in 2001 about 2.2 million households will be headed by a retiree or survivor. The number of households headed by beneficiaries over the age of 64 will grow from one million in 2001 to about 1.2 million in 2010. The estimated number of households headed by beneficiaries under age 65 is expected to remain relatively constant over the 10-year period at 1.2 million. CBO estimates that about 18 percent of beneficiary households are already eligible for FEHB because either the prime beneficiary or spouse already works for the federal government. As a result, those households are not reflected in the estimated cost of H.R. 4030.

CBO estimates that 34 percent of beneficiaries under age 65 who are not already eligible would enroll in FEHB if H.R. 4030 is enacted. Using data from the *1998 Health Care Survey of DoD Beneficiaries* and the *Current Population Survey (*March 1997), CBO estimates that roughly 50 percent of military retirees who are working in a second career for the federal government currently choose to pay an out-of-pocket premium to enroll in FEHB. They do this despite being eligible for Tricare Standard or Extra, for which there is no such premium. New beneficiaries under H.R. 4030 would face the same choice. The estimated participation rate is lower than 50 percent because, according to data from the *1997 Health Care Survey of DoD Beneficiaries*, almost 25 percent of retirees under age 65 have employer-sponsored insurance that requires no out-of-pocket premiums.

For beneficiaries over age 64, CBO estimates that 57 percent of those not already eligible would enroll in FEHB. When military retirees working for the federal government become eligible for Medicare, and thus lose their Tricare eligibility, a greater percentage choose to enroll in FEHB. At the same time, the percentage of retirees who receive free employer-sponsored insurance drops dramatically. The higher estimated participation rate (57 percent) reflects the greater cost of insurance that military beneficiaries face after they turn 65.

Currently, DoD and the Office of Personnel Management (OPM) are conducting a pilot program that allows military retirees age 65 and over to enroll in FEHB for a two-year period. Although enrollment rates have been extremely low, CBO does not believe these rates are representative of what would happen if H.R. 4030 became law. CBO believes that the temporary nature of the program is the primary reason participation rates are low. According to data from the *1997 Health Care Survey of DoD Beneficiaries*, about 55 percent of retirees and survivors currently purchase some form of medigap insurance. Those who enroll in the FEHB demonstration program may not be aware that they can reacquire their medigap coverage at the end of two years, which would explain why so many are reluctant to enroll in the plan.

Premium Costs. CBO estimates the FEHB costs by using the premium rates published by OPM for 2000. The government pays a fixed amount equal to 72 percent of the average premium (weighted by participation in the various plans), but not more than 75 percent for any plan. For both Blue Cross/Blue Shield (BCBS) High and Standard plans, the government's share is $2,050 for an individual policy and $4,575 for a family policy. For Kaiser Permanente's Mid-Atlantic policies, the government's share is $1,900 and $4,575, respectively.

Averaging across plans, the estimated cost to the federal government in 2001 would be $2,177 for individuals and $4,955 for families. CBO estimates that about 80 percent of enrollees would choose a fee-for-service plan like BCBS, and about 20 percent would opt for a managed care plan. Those percentages correspond to actual enrollment data for Civil Service retirees who are currently enrolled in FEHB.

Risk Pooling. H.R. 4030 would place new beneficiaries in a separate risk pool to insulate current FEHB enrollees from any potential increase in premiums. New beneficiaries under H.R. 4030 would be considerably older than the corresponding pool of federal civilian enrollees. Based on self-reported evaluations, the health status of the potential beneficiaries is somewhat poorer than for current FEHB enrollees. However, CBO believes that these differences will have a small effect on premiums for new beneficiaries.

Over 50 percent of CBO's projected enrollees are over age 64 and eligible for Medicare; about 90 percent enroll in Medicare Part B. When retirees are covered jointly by Medicare and FEHB, Medicare pays first and FEHB acts as a wrap-around policy, which significantly lowers the costs to FEHB. For example, under current law annuitants who are covered by Medicare and active employees cost the federal government about the same per capita amount for FEHB. In absolute terms, annuitants cost a lot more, but since Medicare is first payer the actuarial costs to FEHB are about equal for both groups. This group of potential beneficiaries is somewhat more likely to require health care services than current FEHB enrollees, but since Medicare is first payer the effect on premiums is probably negligible.

Beneficiaries under 65 would have a slightly larger impact because the population contains few retirees under age 45. The new pool would not have enough younger people to offset the higher average medical costs for those between 45 and 65. Because those already working for the federal government and those with free employer-sponsored insurance are not included in the new pool, a relatively higher percentage of new beneficiaries choosing FEHB would be in poor health. But, new beneficiaries would bear any increase in premiums, because the government's contribution is limited to the amount paid in the regular FEHB pool.

Additional Medicare Costs. Allowing military retirees the opportunity to enroll in FEHB plans or to use Tricare insurance would also increase costs to the Medicare program. CBO estimates that the FEHB provision of H.R. 4030 would increase Medicare costs by $150 million in 2001, by $1.9 billion over the 2001-2005 period, and by $5 billion over the first 10 years. This increase would stem from increased use of health care by those retirees for whom FEHB/Tricare provides better insurance than they currently receive. In addition, some retirees would seek care from private providers instead of an MTF once they have a generous health insurance plan.

Retirees enrolled in Medicare who do not have a medigap plan or employer-sponsored insurance are likely to increase their use of health care, once they receive supplemental insurance. CBO estimates that this group makes up roughly 13 percent of beneficiaries who are over the age of 64 and who do not currently use MTFs for their medical care. The estimate is based on the *1997 Health Care Survey of DoD Beneficiaries*, which provides self-reported data on private insurance coverage. Although Medicare is currently the primary payer for these people, it would have to pay more because more generous insurance encourages more use of health care services. Using data from published research, CBO estimates that Medicare costs for these individuals would rise by about 25 percent as they gain better coverage.

Many retirees seek health care at MTFs, but there is a significant amount of variation in the degree to which those people use MTFs. With the provision of better insurance fewer people would use MTFs and would turn instead to the private sector. This shift in the provision of care would increase costs to Medicare, which is the first payer under most health insurance policies. CBO estimates that about 3 percent of beneficiaries over age 64 would effectively begin using private health care providers rather than the military health system.

Medicare Subvention. DoD provides health care to almost 350,000 retirees and survivors who are over age 64 and eligible for Medicare. This health care is provided at MTFs on a space-available basis and includes some services that Medicare does not cover, primarily prescription drugs. Under current law, DoD cannot bill Medicare for the cost of providing health care to those beneficiaries over age 64 except in a demonstration project.

The Congress authorized a demonstration project at up to six sites beginning in January 1998 and ending in December 2000. Under that demonstration, DoD provides care to Medicare-eligible beneficiaries and is reimbursed under certain conditions by the Health Care Financing Administration (HCFA), which administers Medicare. The most important condition is the requirement that DoD maintain a level of effort; any additional care is reimbursable by HCFA up to a cap set in law. This care and reimbursement procedure is known as Medicare subvention.

Section 3 of H.R. 4030 would increase the number of sites where HCFA reimburses DoD for care, make the demonstration project permanent, and allow DoD to be reimbursed as a fee-for-service provider instead of the current adjusted rate for managed care that DoD now receives. CBO estimates that these provisions would cost $20 million in 2001 and $945 million over the 2001-2010 period.

In the current subvention demonstration project, enrolled retirees use substantially more care than civilian retirees enrolled in health maintenance organizations. While the high use rate might decline somewhat in a nationwide program, CBO expects that DoD would provide more care to those enrolled in a subvention program relative to the civilian population. Current Medicare-eligible retirees who now receive space-available care at MTFs and choose not to enroll in the subvention program would use the MTFs less frequently. Those retirees would receive more care in the private sector, which would raise costs in the Medicare program.

Survivor Benefits. Retirees of the military, Coast Guard, Public Health Service (PHS), and National Oceanic and Atmospheric Administration (NOAA) are entitled to provide their survivors a government subsidized annuity of up to 55 percent of some chosen base amount, which may not exceed the retirees' base pay. Under current law, when the survivor reaches 62 years of age, the annuity is reduced to 35 percent of the base amount or, if the sponsor was eligible to retire before fiscal year 1986, by the amount of any survivor benefit under Social Security. Section 4 of H.R. 4030 would eliminate this reduction. CBO estimates that the cost of this section would be $543 million in 2001, $3,327 over the 2001-2005 period, and about $8,300 over the 2001-2010 period.

Based on information from DoD, the Coast Guard, PHS, and NOAA, CBO estimates that there will be about 235,000 Survivor Benefit Plan (SBP) annuitants age 62 and older in 2001. About 188,000 or 80 percent of those annuitants currently receive less than the full 55-percent annuity and would receive an increase to that level. Under the bill, those individuals would receive an average increase of $2,900 in 2001. By 2010, CBO estimates that 286,000 annuitants would receive an average annual increase of almost $4,000. CBO estimates that the costs of section 4 would grow primarily for the following reasons:

- The aging of the retiree population over the next several years will lead to a greater number of SBP annuitants;

- The percentage of annuitants aged 62 and older whose annuities would increase under the bill will grow from 80 percent to about 95 percent over the next 10 years. Currently, many of the older annuitants do not receive a Social Security annuity and thus their survivor benefits are not reduced below the 55-percent maximum. As the pool of annuitants becomes weighted more towards those with Social Security benefits the cost of section 4 would increase; and

- The average increase in the annuity would grow by annual cost-of-living increases.

Spending Subject to Appropriation

The impact of H.R. 4030 on spending subject to appropriation would stem from the provisions on FEHB coverage and survivor benefits, which also have effects on direct spending, and from a provision to raise military pay.

Military Pay Raise. Section 2 of H.R. 4030 would raise basic pay by 4.8 percent at a total increase over the 2000 level of about $2 billion in 2001. Because this pay raise would be 1.1 percent above what is projected under current law, CBO estimates that the incremental costs would be $460 million in 2001 and average about $750 million annually over the 2001-2010 period (see Table 3).

Survivor Benefits. Section 4 would increase the annuities of most survivors 62 years of age and older. The military retirement system is financed in part by an annual payment from appropriated funds to the military retirement trust fund, based on an estimate of the system's accruing liabilities. If the bill is enacted, the yearly contribution to the military retirement trust fund (a DoD outlay in budget function 050) would increase to reflect the added liability from the increase in annuities to survivors of future retirees. That payment is discretionary because it depends on whether and how much funding is made available each year for military personnel. Using information from DoD, CBO estimates that implementing this bill would increase such payments by $314 million in 2001, $1.7 billion over the 2001-2005 period, and $3.7 billion over the 2001-2010 period, subject to appropriation of the necessary amounts. (See the discussion of this provision under the heading of direct spending for its other costs.)

TABLE 3. ESTIMATED SPENDING SUBJECT TO APPROPRIATION FOR MILITARY PERSONNEL UNDER H.R. 4030

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
SPENDING SUBJECT TO APPROPRIATION						
Spending Under Current Law						
Estimated Authorization Level[a]	73,692	76,794	79,136	81,560	84,043	86,524
Estimated Outlays	72,580	75,789	78,393	80,946	83,405	88,776
Proposed Changes						
Military Pay Raise						
Estimated Authorization Level	0	478	672	700	727	756
Estimated Outlays	0	460	665	699	726	755
Survivor Benefits						
Estimated Authorization Level	0	314	326	339	351	364
Estimated Outlays	0	314	326	339	351	364
Subtotal-Proposed Changes						
Estimated Authorization Level	0	792	998	1,039	1,078	1,120
Estimated Outlays	0	774	991	1,038	1,077	1,119
Spending Under H.R. 4030						
Estimated Authorization Level[a]	73,692	77,586	80,134	82,599	85,121	87,644
Estimated Outlays	72,580	76,563	79,384	81,984	84,482	89,895

a. The 2000 level is the amount appropriated for that year. The amounts for 2001 through 2005 assume that appropriations are adjusted annually for military pay raises under current law.

Defense Health Programs. H.R. 4030 would generate savings in the military health care system because beneficiaries who enroll in FEHB would likely visit MTFs less frequently and those under 65 would use Tricare less intensely. As detailed in Table 4, CBO estimates that the bill would generate discretionary savings of about $84 million in 2001, about $1.2 billion over the 2001-2005 period, and $3.2 billion over the 2001-2010 period. (See the discussion of this provision under the heading of direct spending for its other budgetary effects.)

Retirees Under Age 65. Those retirees and survivors under age 65 who would enroll in FEHB would still be able to use Tricare Standard or Extra and the MTFs on a space-available basis. When military beneficiaries have dual coverage, Tricare is second payer on all insurance claims. CBO estimates that in a steady state about 330,000 users under the age of 65 would be covered by FEHB. According to DoD estimates, the cost of direct patient care and Tricare use for these beneficiaries is about $1,708 per person. CBO estimates that DoD would save about 75 percent of those costs, since Tricare would still be responsible for covered individuals as second payer. CBO estimates that savings for beneficiaries under 65 would be $49 million in 2001, $656 million over the 2001-2005 period, and about $1.8 billion over the 2001-2010 period.

Retirees Age 65 and Over. Retirees who would enroll in FEHB would use the MTFs less frequently because of better health care coverage. CBO estimates that roughly 20,000 users would leave the military health care system in 2001 and about 48,000 users would leave by 2010. According to DoD estimates, the costs of direct patient care for these beneficiaries averages $2,340 per person. CBO estimates that outlay savings from reduced use of MTFs by retirees over age 64 would be $35 million in 2001, $503 million over the 2001-2005 period, and about $1.4 billion over the 2001-2010 period.

TABLE 4. ESTIMATED SPENDING SUBJECT TO APPROPRIATION FOR DEFENSE HEALTH PROGRAMS UNDER H.R. 4030

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
SPENDING SUBJECT TO APPROPRIATION						
Spending Under Current Law						
Estimated Authorization Level[a]	16,500	16,500	16,500	16,500	16,500	16,500
Estimated Outlays	16,500	16,500	16,500	16,500	16,500	16,500
Proposed Changes						
Estimated Authorization Level	0	-96	-188	-275	-315	-338
Estimated Outlays	0	-84	-174	-262	-306	-333
Spending Under H.R. 4030						
Estimated Authorization Level[a]	16,500	16,404	16,312	16,225	16,185	16,162
Estimated Outlays	16,500	16,416	16,326	16,238	16,194	16,167

a. The 2000 level is the estimated amount appropriated for that year for defense health programs. The current law amounts for the 2001-2005 period assume that appropriations remain at the 2000 level, without adjustment for inflation. If they are adjusted for inflation the base amounts would increase by about $400 million a year, but the estimated changes would remain as shown under "Proposed Changes."

PAY-AS-YOU-GO CONSIDERATIONS

The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in outlays that are subject to pay-as-you-go procedures are shown in Table 5. For the purposes of enforcing pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

TABLE 5. ESTIMATED IMPACT OF H.R. 4030 ON DIRECT SPENDING AND RECEIPTS

	By Fiscal Year, in Millions of Dollars										
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Changes in outlays	0	1,913	3,327	4,738	5,392	5,822	6,285	6,750	7,243	7,760	8,315
Changes in receipts	Not applicable										

PREVIOUS CBO ESTIMATES

CBO recently prepared estimates for five other bills that address DoD's health care programs. Three of those bills, H.R. 2966, H.R. 3573, and S. 2003, address participation by military retirees, their dependents, and their survivors in FEHB. The other two bills, H.R. 3655 and S. 2087, address both participation in FEHB and Medicare subvention. The differences in the estimates reflect the differences in the bills.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

Section 3 of the bill would require insurers, under certain circumstances, to issue medigap policies to Medicare enrollees who chose to drop coverage from DoD's Tricare Senior Prime program. The bill would also prohibit insurers from discriminating in the pricing of such policies based on an individual's health status or use of care, or from using coverage exclusions for preexisting conditions as long as any lapse in coverage was no more than 63 days. These requirements would be private-sector and intergovernmental mandates as defined in the Unfunded Mandates Reform Act. However, because of the relatively low number of people that could be affected by the provisions, the direct costs of the mandates would not exceed the thresholds specified in UMRA ($109 million in 2000 for the private-sector impact and $55 million in 2000 for the intergovernmental impact, adjusted annually for inflation).

ESTIMATE PREPARED BY:

Federal Costs:
Medicare Subvention—Tom Bradley
Survivor Benefits Program—Sarah Jennings
Defense Health Care—Sam Papenfuss
Military Compensation—Dawn Regan

Impact on State, Local, and Tribal Governments: Leo Lex

Impact on the Private Sector: Rachel Schmidt

ESTIMATE APPROVED BY:

Peter H. Fontaine
Deputy Assistant Director for Budget Analysis